

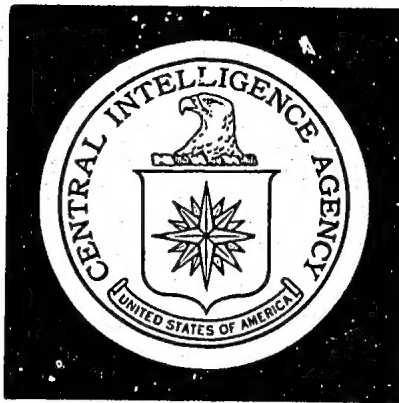
Sanitized Copy Approved for
Release 2010/03/05 :
CIA-RDP85T00875R00170002

Sanitized Copy Approved for
Release 2010/03/05 :
CIA-RDP85T00875R00170002

CIA/OER/IM 71-194

Confidential

25X1



DIRECTORATE OF
INTELLIGENCE

Intelligence Memorandum

East Asia's Changing Textile Industry

Confidential

ER IM 71-194
September 1971

Copy No. 73

WARNING

This document contains information affecting the national defense of the United States, within the meaning of Title 18, sections 793 and 794, of the US Code, as amended. Its transmission or revelation of its contents to or receipt by an unauthorized person is prohibited by law.

GROUP 1
Excluded from automatic
downgrading and
declassification

CONFIDENTIAL

25X1

CENTRAL INTELLIGENCE AGENCY
Directorate of Intelligence
September 1971

INTELLIGENCE MEMORANDUM

EAST ASIA'S CHANGING TEXTILE INDUSTRY

Introduction

1. East Asia's textile industry has developed rapidly over the past decade, stimulated largely by its access to the US market. Textile sales to the United States have boomed, and US efforts to negotiate agreements limiting Japanese shipments of manmade and woolen textile products have thus far been relatively ineffective. In July 1971 the Japanese implemented a "voluntary" restraint program on exports to the United States, and Hong Kong recently announced adoption of its own restraint program. In both cases, however, the controls fall far short of earlier US demands. US negotiations with Taiwan and South Korea meanwhile have not yet brought any results. This memorandum examines key aspects of East Asia's textile industry, its development over the past decade, describes its role in the US and other major foreign markets and assesses the likely impact of export controls. Three appendixes dealing with the textile industries in Hong Kong, Taiwan, and South Korea are included to elaborate on the general assessment made in the body of the memorandum.

25X1

Discussion

The Revolution in World Textiles

2. Textile production around the world has historically been based on processing natural fibers, mostly cotton. The only significant change

Note: This memorandum was prepared by the Office of Economic Research and coordinated within the Directorate of Intelligence.

CONFIDENTIAL

25X1

CONFIDENTIAL

prior to the 1960s was the introduction of rayon on a fairly large scale after World War II. Although rayon production increased sharply during the 1950s, natural fibers remained the backbone of textile production in virtually every country. As late as 1960, cotton accounted for roughly two-thirds of world yarn production, and together with wool made up more than three-quarters of fiber consumption.

3. By the start of the 1960s, however, synthetic fibers had gained commercial acceptance. With this growing popularity came a major change in the textile industry as synthetic fibers and blends of synthetics and natural fibers made sharp inroads in world markets. In fact, most of the growth in textile production over the past decade has been in synthetics. Between 1960 and 1969, total synthetic fiber production increased more than 520% while cotton and wool yarn output together grew by less than 10%. In the United States, the largest single consuming country, mill consumption of natural fibers actually declined while synthetics rose by about 15% a year.

4. The shift to synthetics is particularly evident in world trade. By the end of the 1960s, manmade fiber textiles accounted for more than two-fifths of total world trade in manufactured textile products,⁽¹⁾ compared to an almost insignificant share during the late 1950s.⁽²⁾ This rapid growth primarily reflects the shift in consumer demand to synthetics, which incorporate properties natural fibers lack. Increased import restrictions on cotton textiles by major foreign markets also played a role. As early as the mid-1950s the United States and European Community (EC) countries were limiting cotton textile imports, and by the mid-1960s controls covered virtually every important market. Synthetic textiles remained relatively free of import restrictions, however, and those exporting countries shifting into synthetics increased their textile sales sharply.

5. Not all exporters have shifted. Most industrial countries, especially the United States and Japan, moved rapidly into synthetics, but only a few less developed countries have done so. India and Pakistan, which have the largest textile industries among this group, remain basically cotton textile producers, geared primarily to supplying domestic markets with inexpensive textiles. The same is true of the Soviet Union and Communist China. Indeed, outside the industrialized Free World countries, only Hong Kong, Taiwan and South Korea have moved rapidly into synthetics.

1. For the purposes of this memorandum, manufactured textile products exclude natural fiber raw materials.

2. All reference to world textile trade in this memorandum excludes intra-EC trade.

CONFIDENTIAL

CONFIDENTIAL

The Dynamics of East Asia's Textile Industry⁽³⁾

6. East Asian producers – Japan, Hong Kong, Taiwan, and South Korea – comprise the world's largest textile exporting group, with sales of nearly \$4 billion last year (see Figure 1). By the end of the 1960s the four accounted for almost one-third of total world exports of manufactured textile products, and their relative importance is still growing rapidly. Hong Kong, Taiwan, and South Korea have accounted for almost all the growth in textile exports from less developed countries during the past decade and now have more than two-thirds of total textile exports by less developed countries. Japan, on the other hand, is by far the largest exporter among developed countries, selling about one-fourth of the total.

7. By and large the textile industries in East Asian less developed countries were started because a well-disciplined, energetic, and low-wage labor force was available. In a labor-intensive industry such as textiles, this is a marked advantage. At the same time, East Asian textile manufacturers are a dynamic and enterprising group who adapt readily to changing world conditions. This is reflected in their dramatic shift to synthetics in just a few years. As recently as 1965, Hong Kong, Taiwan, and South Korea were almost exclusively producers and exporters of cotton and woolen textiles, but by 1970 roughly 40% of their combined exports were synthetics, including some rayons.

8. The move into synthetics led to a major expansion of their textile industries. During the early 1960s, textile production increased modestly, but output has boomed since 1965. Taiwan and South Korea more than tripled their textile output in five years, and Hong Kong did almost as well (see Figure 2). All three are rapidly modernizing by introducing new equipment and by upgrading product lines. Hong Kong, for example, is moving away from low-value undergarments and toward higher quality outerwear. Taiwan and South Korea still concentrate on low-quality items such as white shirts and inexpensive sweaters, but they too are shifting.

9. The growth of Japan's well-developed textile industry also accelerated during the latter 1960s. This largely reflected a move into synthetics. The industry also has been undergoing a structural transition from a labor-intensive to a more capital-intensive industry. The changeover has been assisted by a government-directed program designed to eliminate surplus spindles, modernize weaving equipment, and increase efficiency essentially by mergers. This modernization program was a reaction to rising

3. For the purposes of this memorandum, the textile industry includes all phases of processing from synthetic fiber production to apparel production.

CONFIDENTIAL

CONFIDENTIAL

labor costs, a growing manpower shortage, and intensifying competition from other East Asian producers.

10. The expansion of East Asia's textile industry was made possible by a largely unfettered access to the US market. Although cotton textile imports have long been restricted, there are no restrictions on importing synthetics. This is in marked contrast to other major markets such as the EC. East Asian textile sales to the United States more than doubled between 1965 and 1970 (see Figure 3), with Hong Kong, Taiwan, and South Korea recording spectacular gains – an eightfold increase in the case of Taiwan. Japan's exports to the United States grew a modest 7.5% annually, but the Japanese also gained from the success of the other East Asian producers by selling them increasing amounts of textile machinery, fabrics, yarns and synthetic fibers (see Figure 4), which in turn are manufactured into made-up goods for export mainly to the United States. South Korea and Taiwan buy almost all their manufactured textile products from Japan, and Hong Kong buys about half. These three are Japan's most rapidly expanding major overseas textile markets and collectively buy almost as much as does the United States (see the map, Figure 5).

11. The phenomenal growth in textile exports to the United States by the smaller East Asian producers was partly at the expense of other suppliers (see Figure 6). While total US imports of manufactured textiles rose 90% between 1965 and 1970, imports from Hong Kong, Taiwan, and South Korea jumped by about 300%. Their share of the US import market – more than 25% – is about the same as Japan's. Moreover, in the important apparel and made-up goods category,⁽⁴⁾ which makes up most of their exports, they account for an extraordinary 40% of US imports, and, together with Japan, supply almost two-thirds of the US import market (see Figures 7 and 8).

12. The United States is still Japan's largest overseas market, taking about one-fourth of Tokyo's textile exports. Unlike sales to East Asia, which are mostly fibers, yarns, and fabrics, Japan basically sells finished goods in the US market (see Figure 9). Nearly 60% of its total exports go to the United States. Since 1965, sales of apparel have increased in value by 12% annually, largely by a steady upgrading of the quality of apparel and

4. *For the purposes of this memorandum, non-clothing textile products include: tulle, lace, and embroidery (SITC category 654), special textile fabrics (SITC category 655) and made-up articles of textile materials (SITC category 656.9). For clothing, all trade data in this memorandum exclude clothing accessories of leather (SITC category 841.3) and headgear (SITC category 841.5). All US import data exclude jute fabric (SITC category 653.4).*

CONFIDENTIAL

CONFIDENTIAL

by increasing the volume of higher priced synthetic blend items. The improved product quality accounted for the slight increase in the value of clothing exports last year despite a drop in volume.

The Changing Situation

13. The rapid growth of Taiwan, South Korea, and Hong Kong as major textile exporters is forcing changes both within the region itself and between East Asia and its leading textile trading partners. Competition among the region's exporters is growing and will intensify as the initial boom in synthetics slackens. Meanwhile all East Asian producers are facing the problem of limited access to foreign markets. Exports to the EC are already tightly restricted through a variety of methods, and the United States is pressing for new controls. Other fast-growing foreign markets such as Australia, Canada, and South Africa are also moving in this direction.

14. Rising labor costs are gradually eroding Japan's competitive position. Outside of North America, the Japanese already have one of the highest wage rates in the textile industry, and Japanese wage rates are increasing more rapidly than in most countries (see Figure 10). Stimulated by a growing labor shortage, the industry's wages have risen about 15% annually since 1965, and in 1969 averaged about 90 cents an hour. Although well below the US average of \$3.19 an hour, they are higher than those in France or Italy and three to six times higher than in Hong Kong, South Korea, and Taiwan. The gap almost certainly widened last year when Japanese textile wages jumped by about 20%.

15. With their lower cost structure, the other East Asian countries are cutting deeply into foreign markets, including the United States, where Japan once held a wide edge. Japan has already lost much of its overseas markets for cotton fabrics, and clothing exports are now being adversely affected by competition from other East Asian producers who, in many instances, can undersell the Japanese by 20% to 30%. For a long while, Japan was able to increase its overseas sales by upgrading its product lines as other suppliers moved into the low-quality product market. This is becoming more difficult, however, and in the past year or two, Japan's clothing exports have stagnated while elsewhere in East Asia the boom is continuing.

16. East Asian suppliers are even penetrating Japan's domestic market, although the amounts involved are still small. Japanese imports of manufactured textile products increased sharply in the past year or so, and much of the increased demand for cotton fabric is being met by imports. Clothing imports more than doubled last year, but imports still account for less than 4% of total domestic sales. Practically all of these purchases

CONFIDENTIAL

CONFIDENTIAL

came from East Asia and consisted mostly of low-value items, including many intermediate goods such as pockets and shoulder pads. Tokyo expects textile imports to continue rising, but past experience suggests that controls will be strengthened should imports become a serious threat to the domestic industry. To help protect Japanese producers, for example, few finished textile goods were included in Tokyo's recent tariff cuts for less developed countries.

17. Because of their weakening competitive position, many large Japanese textile firms are investing in companies elsewhere in East Asia where labor costs remain low. The Japanese now jointly own more than 100 overseas firms at least half of which are in East Asia. The size and importance of those operations both to the Japanese and to the host country are reflected in the fact that the Japanese-controlled textile plants abroad account for approximately one-sixth of US textile imports. Most of these plants produce finished goods, but the Japanese are increasingly investing in large synthetic fiber and fabric plants as well.

The Problem of Export Controls

18. The immediate problem facing East Asian textile producers is the prospect of export controls on shipments of synthetic⁽⁵⁾ and woolen fiber products to the United States. These products account for approximately three-fourths of the value of East Asia's total textile exports to the US market and are easily the most rapidly growing items. Last year, synthetic fiber textile goods accounted for all the increase in textile sales to the United States. Because of the importance of synthetics, the three smaller East Asian producers have been reluctant to adopt any new restrictions on sales to the US market, although Hong Kong has begun to implement its own restraint program. Japan began implementing a "voluntary" restraint program on 1 July 1971, but the controls fall far short of earlier US demands for item-by-item restrictions.

19. More than 90% of the value of Japanese textile sales to the United States are covered by their recently initiated "voluntary" export controls. The restraint program covers four major categories - cotton, wool, synthetic fabrics, and finished goods made of those materials. The increase in exports for each group for the year beginning in July 1971 is limited to 5% of the volume of exports during Japan's fiscal year, April 1970 - March 1971. In the two successive years the allowed volume increase would be 6% annually. The Japanese have also imposed ceilings on their exports of several specific textile products.

5. *Including rayons, which constitute a relatively small share.*

CONFIDENTIAL

CONFIDENTIAL

20. Japan's export controls on cotton and wool fabrics will have little or no impact because shipments to the United States have been dropping. In the case of finished goods, growth in the volume of Japanese sales to the United States has recently slowed considerably. US imports of cotton items from Japan have stagnated since 1965 while woolen items, about 2% of finished goods, grew by 8.5% a year. Imports of synthetic fiber finished goods, once the major growth item, have also slowed sharply because of increasing competition from other East Asian producers. Last year, US imports of these items from Japan rose a mere 1% in volume and, despite Japanese efforts to flood the US market before export restraints were imposed, their import volume during the first five months of 1971 was less than 4% above the same 1970 period. Other East Asian suppliers meanwhile continued to register remarkable increases.

21. The only category that could be significantly curtailed by export controls is synthetic fabrics. Since 1965, US imports of synthetic fabrics from Japan have risen more than 12% annually, and the rise accelerated to 29% last year. If the Japanese were to adhere to the scheduled limits on the export growth rate for each category, they would face a significant slowdown in textile exports to the United States. However, we believe that Tokyo will shift unused portions of quotas to other categories. The likely decline or stagnation in exports of cotton and woolen fabrics, for example, means that a significant portion of their quota will be left unused. This portion can be reallocated to the synthetic fabrics category. In addition, a substantial portion of the finished goods quota may be available for shifting as well. By such shifts, synthetic fabric exports could continue to increase rapidly. Even in the case of self-imposed export ceilings on specific textile products categories, Tokyo apparently has protected itself by setting very high ceilings. Among the specific items with ceiling limits are synthetic knit fabrics, which accounted for most of the growth in exports to the United States last year. Here, the ceiling reportedly allows a 60% increase in exports during the first year of controls.

22. Japanese textile exports to the United States, therefore, will not likely be very much affected by the voluntary restraints. Given the possibilities for shifting quotas between categories, there is sufficient room for export volumes to grow at near the 6% rate recorded since 1965, and their value could well increase faster as the trend toward upgrading product lines continues. If export growth does fall short of these rates, it will not be due to export controls but rather to competition from other East Asian producers. Japanese textile exports would also be affected if other East Asian producers agree to impose export controls on their shipments to the US market because Japanese sales of intermediate materials to them are closely related to their sales to the United States. But even considering these factors, there is still room for Japan to expand total textile exports

CONFIDENTIAL

CONFIDENTIAL

since the value of Japan's sales to other East Asian producers are growing faster than the volume of their shipments to the US market.

23. Other East Asian producers probably would not be seriously hurt by export controls. In the case of Hong Kong, the Crown Colony has recently decided to impose its own restraint program which would limit textile shipments to about a 6% annual increase. Although all details of the program are not yet available, it apparently allows for practically full shifting between textile fiber products. This limits the impact because US imports of cotton and woolen products from Hong Kong are stagnating or declining. Indeed, despite a 30% increase in imports of synthetic fiber products during 1970, the overall volume of shipments remained virtually unchanged from the 1969 level. During the first five months of 1971 the volume of shipments was up less than 9%, but as in the past the value increased much more as a result of the move to higher quality items. So long as product shifting is allowed, the colony's restraint program allows for substantial growth in textile exports to the US market. Meanwhile, other export markets are likely to continue expanding fairly rapidly and Hong Kong's overall textile exports will probably be able to increase at near the 15% pace of recent years.

24. Taiwan would not be seriously hurt by export controls. In late May 1971, Taipei agreed in principle to restrict export growth to around 10% annually on synthetic and woolen textiles, which make up about 90% of Taiwan's textile exports to the United States. Although this would mean a substantial slowdown from previous years, the impact would vary depending on the base period adopted. Taipei no doubt wants the base period to be 1971 because exports to the United States this year are expected to jump by \$100 million. This base period would allow Taiwan's textile exports to reach at least \$375 million by 1975 as opposed to \$250 million if 1970 were the base year. In any event, sales to other countries are also expected to increase, and, even with added trade restrictions, the textile industry will still have plenty of room to expand.

25. South Korea would probably be hardest hit by export controls since it is the most dependent on the US market. Even so, the industry could probably overcome much of the effects of a 10% limit on volume increases - about half the rate of 1970 - because of the possibility of shifting to higher quality items. Moreover, as with Taiwan the more current the base year used to determine future export volumes, the less severe will be the impact of export controls. How deeply export controls will cut into growth rates will also depend on what happens in South Korea's other major market, Japan, which accounted for one-third of the increase in textile exports since 1965. If sales to the Japanese market continue increasing at past rates, the industry will have little trouble sustaining a rapid growth

CONFIDENTIAL

CONFIDENTIAL

rate. But should Tokyo clamp down on imports, export growth for textiles would slow sharply.

The Longer Term

26. Over the long term, East Asia's textile industry is likely to undergo rapid changes regardless of export controls. The Japanese will suffer further losses as a result of increasing competition from the lower-wage less developed countries in the area as they upgrade their products. Even Japan's present advantage in synthetic fiber yarns and fabrics and some clothing items will erode in time as its competitors acquire the technology and capital to expand their own synthetic industries. This trend will be accelerated by a yen revaluation which gives other East Asian producers a stronger competitive edge over the Japanese in foreign markets as well as in Japan itself. Within the Japanese industry, the losers will be the many small firms which have been unable to modernize their operations; the relatively few very large firms will continue to do well.

27. In terms of the overall economy, Japan's textile industry is already steadily diminishing in importance. This should have beneficial results in the long run. Japan must continue the process of structural change to more capital-intensive industries to maintain a high rate of economic growth. A reduction in the one million textile workers will permit a shift of labor to high-growth industries, helping to alleviate the manpower shortage, which could become a serious limitation in the drive to maintain present growth rates. Indeed, the shift has already begun and is likely to accelerate as more and more small firms leave the industry.

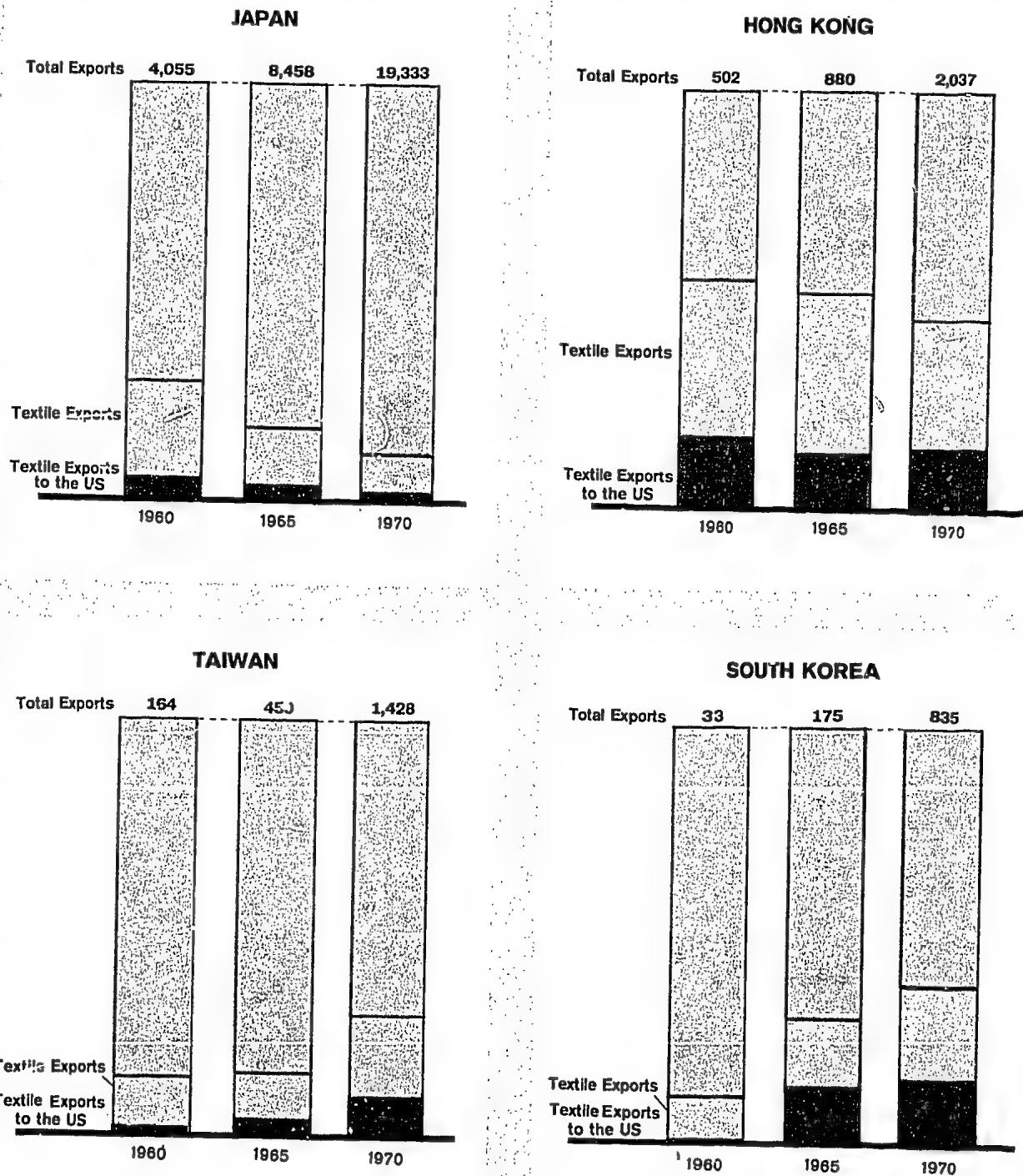
28. Other East Asian producers will probably make further inroads into the US market in the coming years. Even with some decline in the growth of textile sales, however, overall economic activity in the region will be little affected. New growth industries are rapidly emerging and in time will replace textiles in importance. In all three countries, exports of such items as electronic equipment, plastics, and light machinery are already increasing much faster than textiles. Hong Kong, South Korea, and Taiwan all have very dynamic economies, and continued economic growth over the long term depends more on the development of new export industries and products than on the continuing growth of their textile industries.

CONFIDENTIAL

EAST ASIA: Textile Exports

Figure 1

Million US \$



812041, 9-71

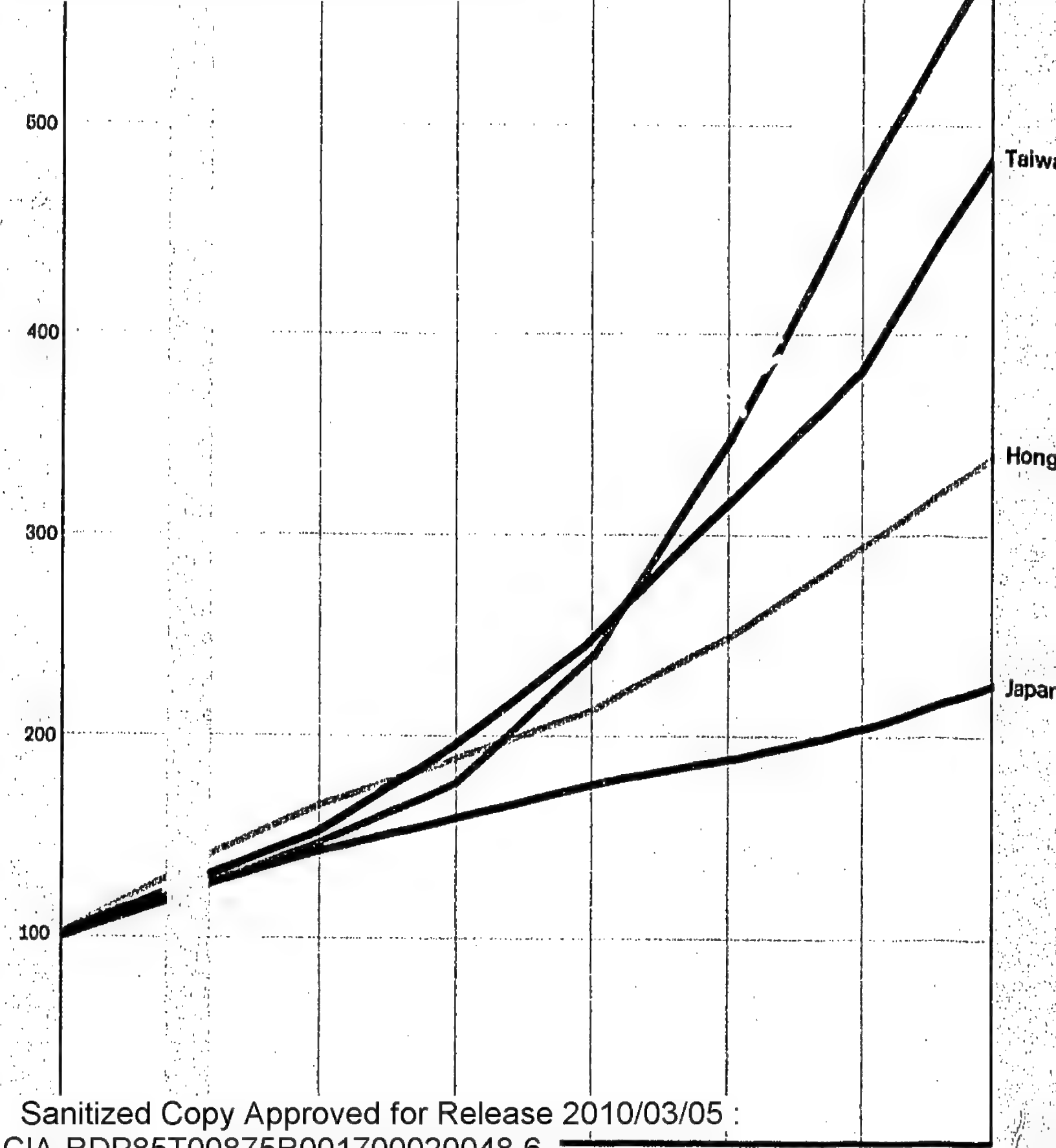


Figure 3

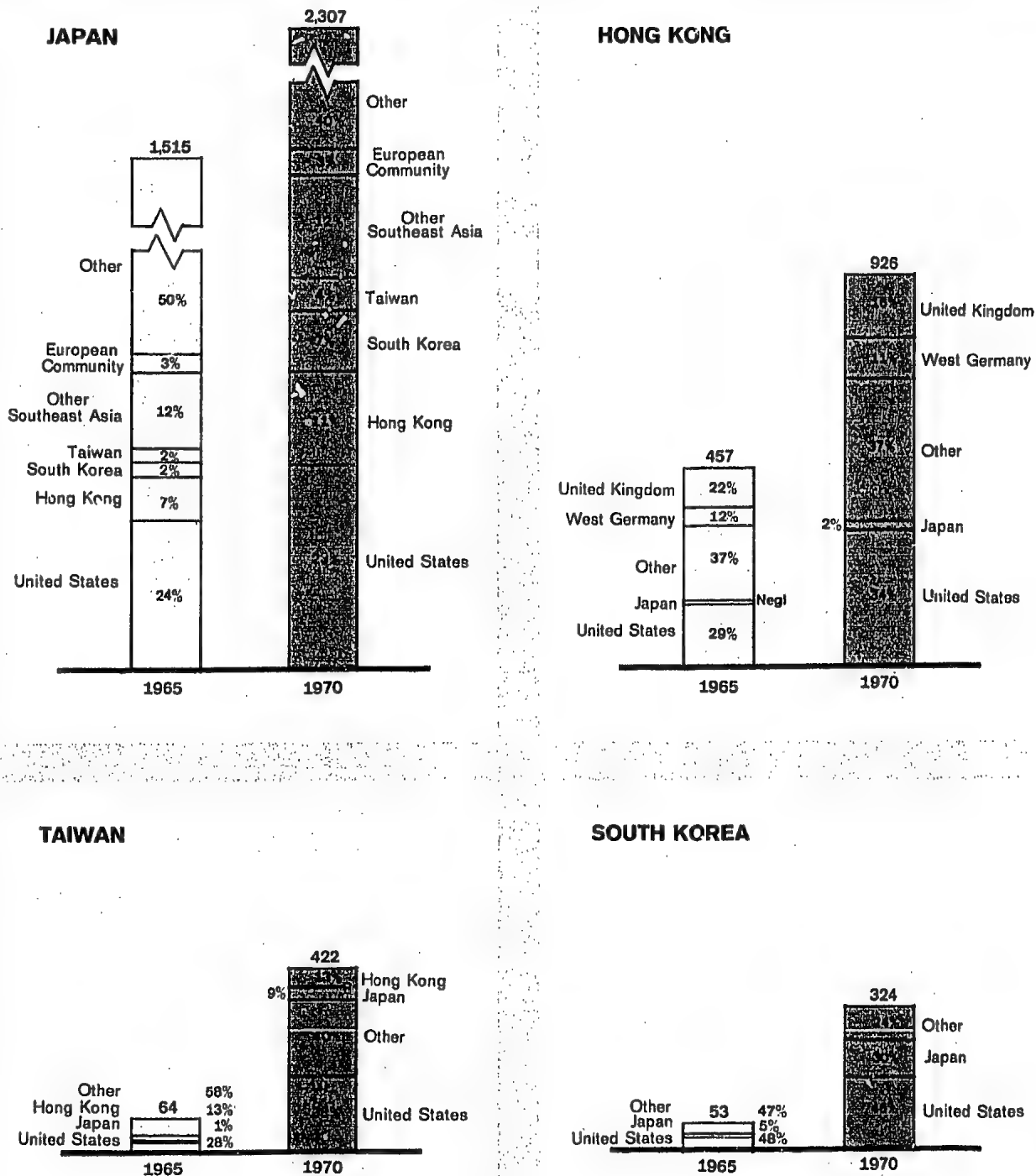
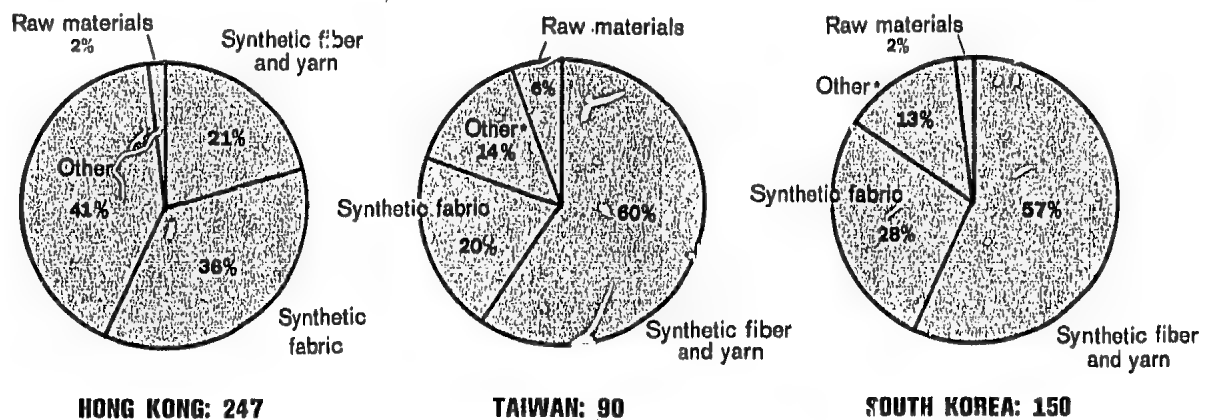
EAST ASIA: Direction of Textile Exports*Million US \$*

Figure 4

Hong Kong, Taiwan, and South Korea Textile Imports, 1970

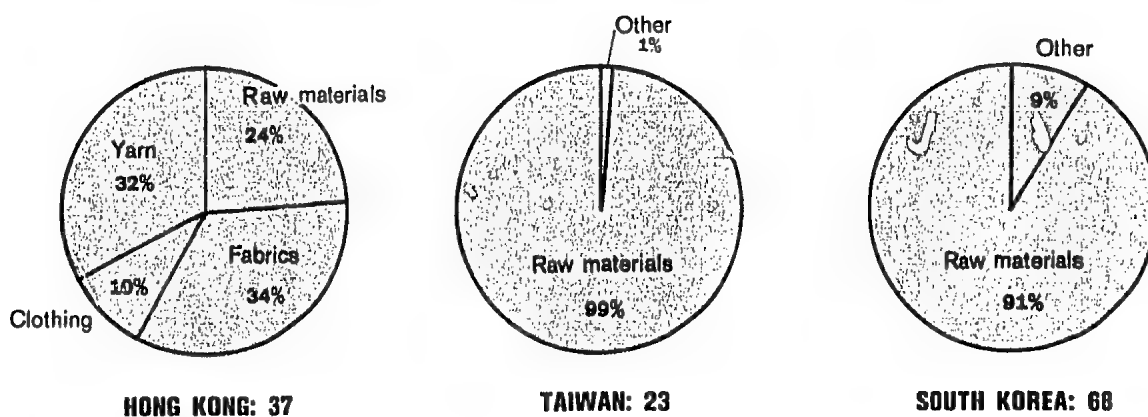
Million US \$

Textile Imports from Japan



*includes mainly non-synthetic fabrics

Textile Imports from the US

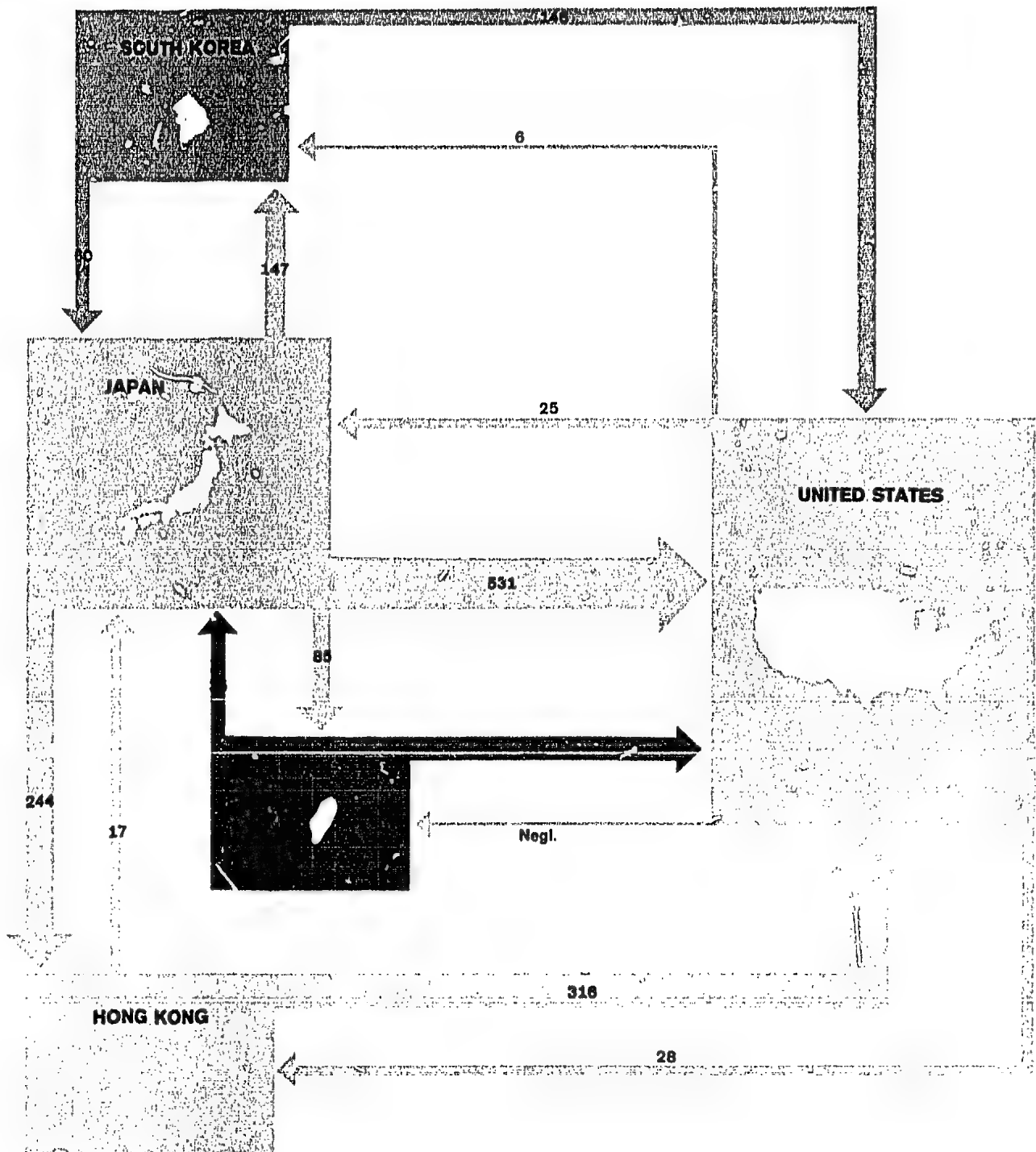


512044 9-71

Figure 5

EAST ASIA: Manufactured Textile Trade Flows, 1970

Million US \$



512045 9-71

Figure 8

US Imports of Manufactured Textile Products

Million US \$

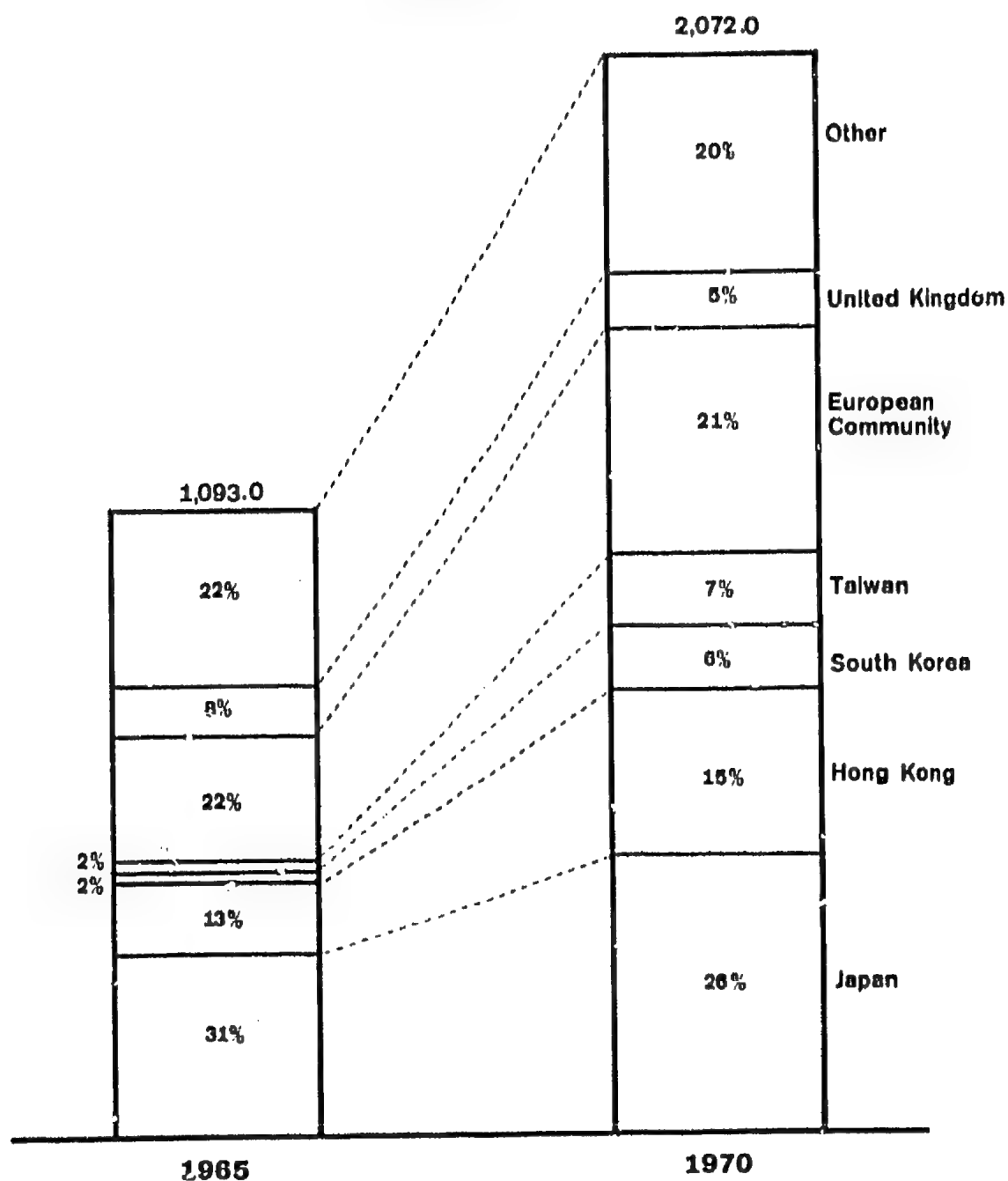
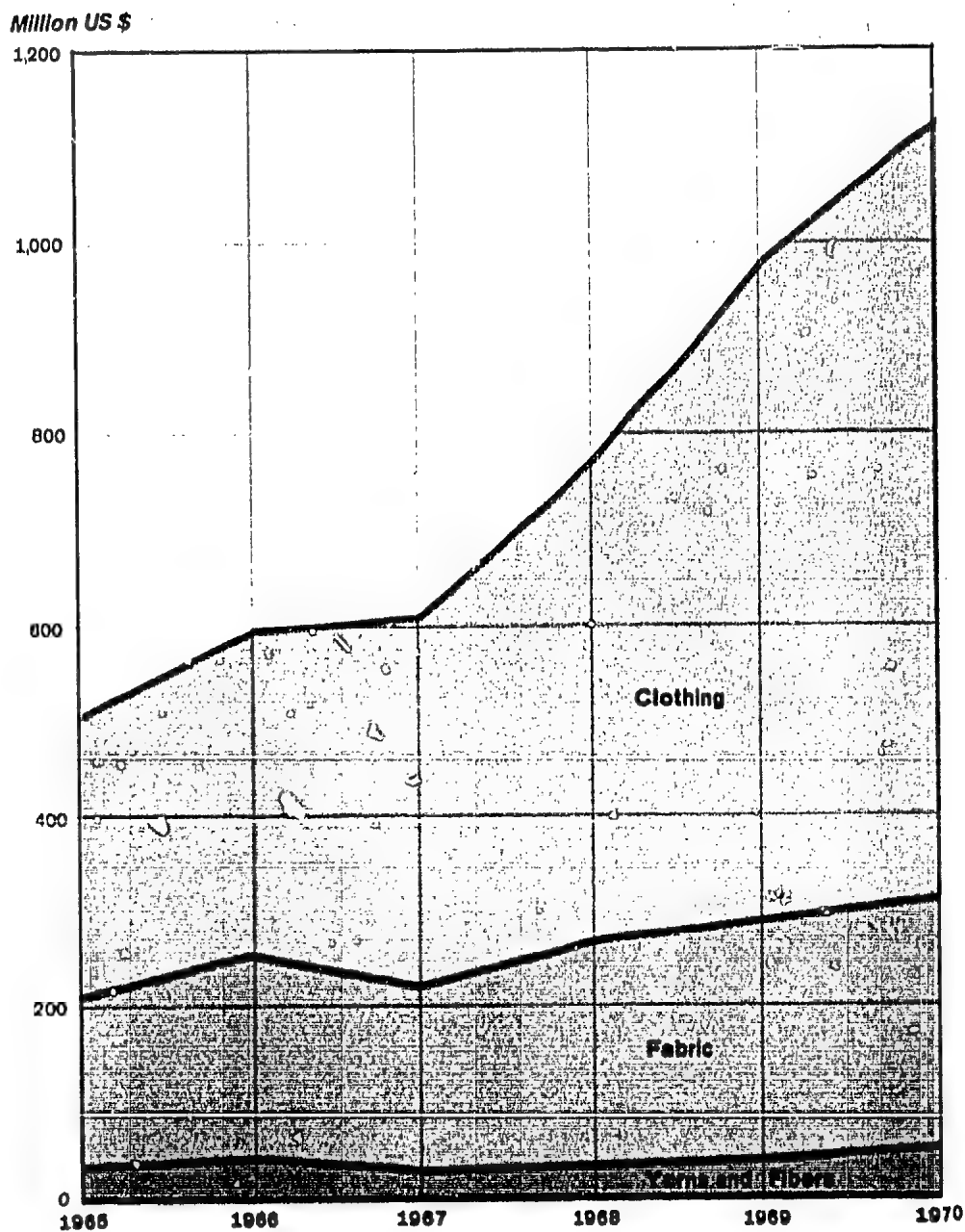


Figure 7

US Imports of Manufactured Textile Products from East Asia

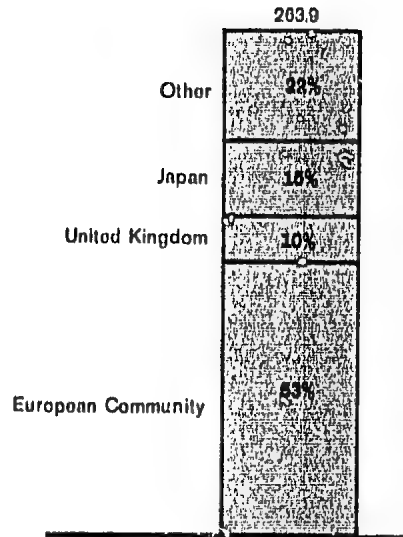


512047 9-71

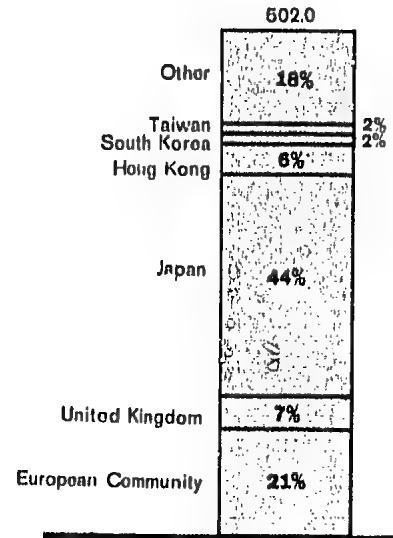
Figure 8

US Imports of Manufactured Textile Products, 1970 *Million US \$*

FIBERS AND YARN



FABRICS



FINISHED GOODS

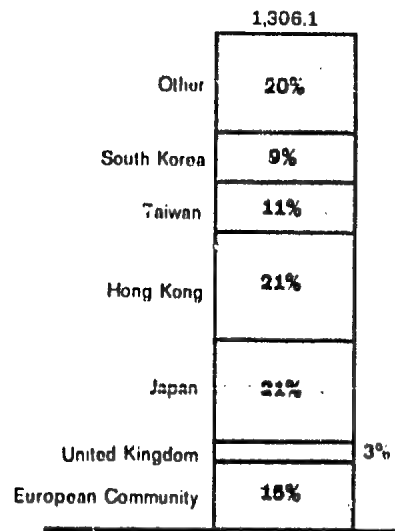


Figure 9

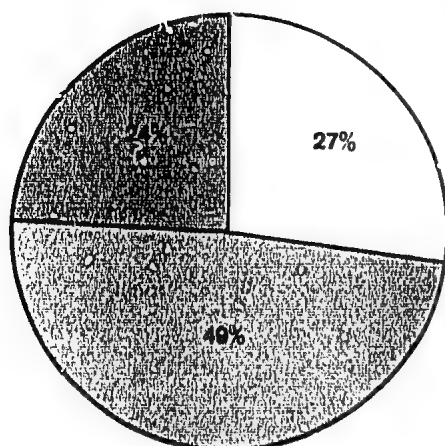
Exports of Textiles by Commodity, 1970

Million US \$

Yarns and fibers

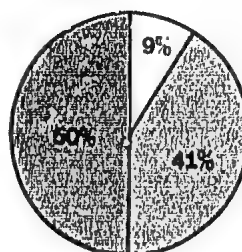
Fabrics

Secondary products

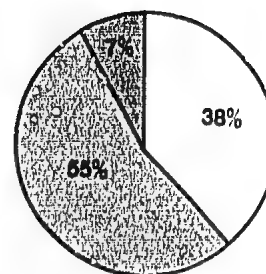


JAPAN

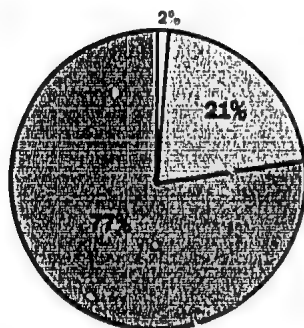
WORLD: 2,307



UNITED STATES: 534



ASIA: 757



HONG KONG

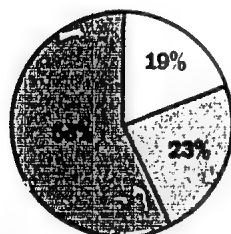
WORLD: 926



UNITED STATES: 316



JAPAN: 17



TAIWAN

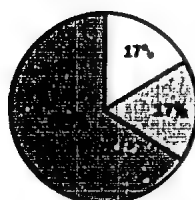
WORLD: 422



UNITED STATES: 161



JAPAN: 35



SOUTH KOREA

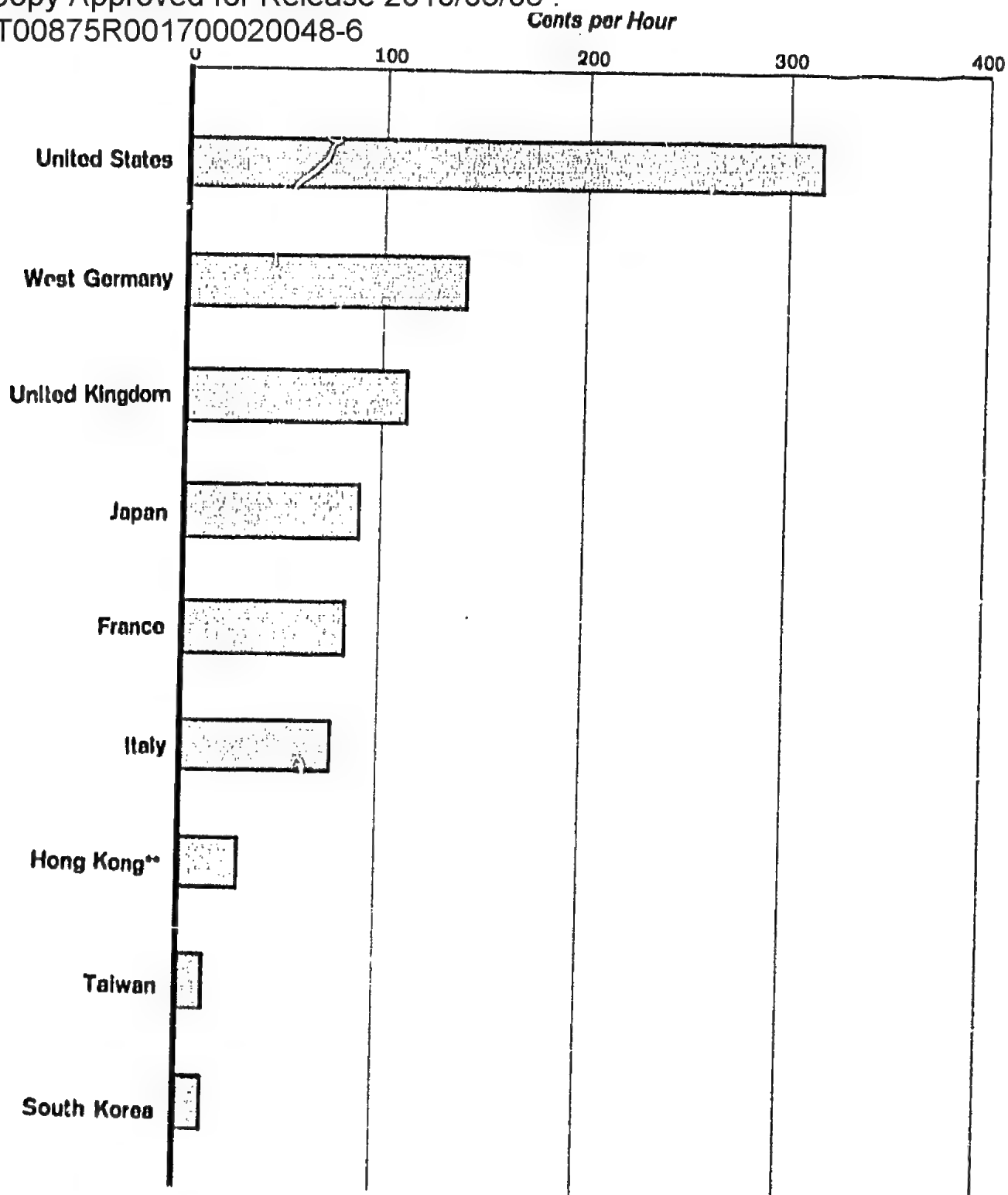
WORLD: 324



UNITED STATES: 149



JAPAN: 96



CONFIDENTIAL**APPENDIX A****Hong Kong's Textile Industry****Size and Scope**

1. Hong Kong is by far the largest textile exporter among less developed countries, accounting for nearly 40% of their total textile exports. It even sells more manufactured textile products abroad than the United States. The industry essentially got started during the early 1950s following the emigration of large numbers of Shanghai weavers to Hong Kong after the Communists took power on the mainland. By providing the capital to set up new plants and the skills to run them, this group formed the nucleus of the textile industry, and the inflow of refugees from China provided a cheap, energetic, and well-disciplined labor force. With all these factors working for it, Hong Kong's textile industry has become the largest in East Asia after Japan and Communist China.

2. After leading the colony's economic growth during most of the post-World War II period, textiles have begun to decline in relative importance in recent years as new growth industries developed. Although textile production has increased sharply since 1965, other export industries such as electronics, plastics, and wigs have grown even faster. Exports of electronic products, for example, increased by 340% between 1965 and 1970 while exports of wigs rose by 1200%.⁽¹⁾ By comparison, textile exports (including clothing) grew by 100%. As a consequence, the textile share of total exports has declined moderately since 1965.

3. Textiles are nonetheless Hong Kong's most important industry. In 1970, textile exports were some \$926 million and represented 45% of all export earnings. About one-fifth of all imports⁽²⁾ are used by the textile industry. Moreover, over 230,000 workers, or more than 40% of the colony's registered industrial labor force, are employed in textile production. Almost one-half are engaged in garment production, which makes up the backbone of the industry. The rest are involved in spinning, weaving, dyeing, and finishing. Altogether there are some 4,600 registered firms producing textiles – about 28% of all registered firms in the colony – plus a large number of unregistered establishments.

1. All export data in this appendix exclude re-exports.

2. Import data in this appendix refer only to retained imports. Some 17% of Hong Kong's total imports are goods resold abroad without alteration.

CONFIDENTIAL

CONFIDENTIAL

4. As in many countries, Hong Kong's textile industry is made up of numerous small firms and a few large ones which account for a large share of production. Almost one-half of the colony's 880,000 spindles, for example, are operated by seven large mills. In the weaving sector, most firms operate less than 100 looms and many as few as 10. Again, a large share of the roughly 23,000 looms are operated by a few big companies. On the other hand, dyeing and finishing as well as garment production are dominated by small-scale, family-type operations, with large firms playing a relatively small role. Most investment capital comes from local Chinese sources and relatively small amounts from the United States, the United Kingdom, and Japan.

5. Hong Kong's textile industry is basically oriented toward producing finished clothing for overseas markets. With a population of only about 4 million persons, the domestic market is limited and takes only a small share of output. The colony's spinning and weaving output is small except in cotton goods. Capital-intensive projects, such as those required in producing synthetic fibers (including a petrochemical industry), have been largely avoided because businessmen fear the Chinese Communists might take over Hong Kong at any time and expropriate their investment. Because of this deficiency in synthetics, Hong Kong is a net importer of both yarns and fabrics.

Production Trends (see Table A-1)

6. Like other dynamic textile industries, Hong Kong's industry is undergoing rapid change. The major development is the trend away from cotton textiles toward synthetics and wools. Until the mid-1960s the industry was based almost completely on producing cotton yarns, fabrics, piece goods, and clothing. While cotton still predominates in the spinning and weaving sectors of the textile industry, its importance is declining rapidly. In fact, since 1968 there has been virtually no increase in pure cotton yarn or fabric production. Output of manmade blends and woolen yarns, on the other hand, has increased by about 66% and 39%, respectively. Sharp increases were recorded for blended fabric production. Moreover, fabric imports consist largely of synthetics or synthetic blends. A growing share of spindles is being adapted to handle synthetic fibers, and an estimated one-fourth of total spindlage is now devoted to mixed yarns.

7. The garment industry has made the greatest progress in shifting to synthetics and other manmade fiber products. Judging from export data - no production data are available - these fibers now account for about one-half of clothing output; in 1965 they represented about 20%. These inroads were made largely at the expense of cotton, but woolen apparel items also declined in importance. Cotton's share dropped from

CONFIDENTIAL

Table A-1
Textile Production

	<u>1960</u>	<u>1965</u>	<u>1967</u>	<u>1968</u>	<u>1969</u>	<u>1970</u>
	<u>Metric Tons</u>					
Yarns						
Cotton	78,520	131,017	137,248	147,492	144,109	148,498
Wool	1,718	7,909	7,932	8,723	11,006	12,092
Cotton blends	122	947	5,755	9,528	13,231	15,843
Manmade (pure)	Negl.	Negl.	Negl.	Negl.	Negl.	3,699
	<u>Thousand Square Yards</u>					
Fabrics						
Cotton	461,482	639,734	723,586	776,670	750,159	757,861
Cotton/rayon	2,053	3,340	11,779	18,980	29,908	34,465
Cotton/synthetic	N.A.	N.A.	20,661	41,505	48,460	47,473
Rayon (pure)	2,185	1,199	1,118	1,425	1,367	1,538
Synthetic	Negl.	Negl.	Negl.	Negl.	Negl.	1,780

CONFIDENTIAL

- 13 -

CONFIDENTIAL

CONFIDENTIAL

about 50% in 1965 to only 30% last year, while woolens fell from 30% to 20% during the same period. The shift to synthetics underlies much of the very rapid increase in clothing exports during the late 1960s. Overall clothing exports more than doubled during 1966-70, with synthetics accounting for about two-thirds of the increase. Last year, exports of synthetic clothing jumped an estimated 42%, while the other types actually declined.

8. The garment industry has also benefited by shifting to new product lines and upgrading the quality of existing ones. Over the past half decade or so, increasing emphasis has been placed on producing outerwear rather than concentrating on shirts and underwear, which stimulated much of the industry's growth during the 1950s and early 1960s. Such items as jackets, suits, and women's dresses, for example, now account for about two-thirds of total clothing exports, compared with about one-half in the early 1960s. Underwear and accessories, which made up almost one-third of clothing exports in the early 1960s, now make up less than 20%. Shirts have also declined in importance, from 19% to 17% of clothing sales. Even in this category, the emphasis is now on permanent-press dress shirts, and the value of shirt sales consequently has been increasing about 50% faster than the volume.

Trade Trends (see Tables A-2 and A-3)

9. Aided by the booming apparel industry, Hong Kong has been able to maintain the textile export growth rate at about 15% annually since 1965. The growth rate fell slightly last year to 13%, primarily because of the drop in sales of cotton and woolen clothing items. Even so, with synthetics growing rapidly, clothing has increased its share of total textile exports to 77%, with yarns and fabrics making up most of the balance. The share of exports of non-clothing items fell fairly steadily during the latter 1960s, as sales rose by only about 7% annually compared with 18% for clothing items.

10. Since the mid-1960s the United States has been Hong Kong's largest overseas market for textiles and the fastest growing of the major markets. Hong Kong's textile exports to the US market have increased at an average annual rate of 19% since 1965 in spite of a sharp drop to about 9% last year, caused in part by increasing competition from Taiwan and South Korea. The United States now takes about one-third of Hong Kong's textile exports; its purchases were valued at about \$316 million last year. Hong Kong is the largest supplier of textiles to the US market after Japan, accounting for about 15% of US manufactured textile product imports in 1970. This share was about 13% in 1965.

CONFIDENTIAL

Table A-2
Hong Kong: Textile Exports

	Million US \$					
	1960	1965	1967	1968	1969	1970
<i>Total</i>	274	457	566	668	818	926
Yarns			15	14	19	23
Fabrics	98	149	119	124	134	153
Non-clothing products			29	33	33	34
Clothing	176	308	403	497	632	716

CONFIDENTIAL

- 15 -

CONFIDENTIAL

Table A-3

Hong Kong: Textile Exports to the United States

	Million US \$					
	<u>1960</u>	<u>1965</u>	<u>1967</u>	<u>1968</u>	<u>1969</u>	<u>1970</u>
<i>Total</i>	84	133	176	242	290	316
Yarns	Negl.	Negl.	Negl.	Negl.	Negl.	Negl.
Fabrics		24	27	31	32	32
Non-clothing products	84	-	7	10	11	11
Clothing		109	142	201	247	273

CONFIDENTIAL

- 16 -

CONFIDENTIAL

CONFIDENTIAL

11. More than four-fifths of textile exports to the United States consist of clothing, which was valued at \$273 million in 1970. Hong Kong is easily the largest single source of US clothing imports, accounting for about 23% of the total. For many specific items, its share is much higher. Among manmade fiber products, for example, Hong Kong accounts for 42% of US imports of knit blouses and about 30% of woven dress shirts. In volume terms, it accounts for about 35% of US imports of woolen apparel, but its value share is much less because of higher-quality goods coming from Western Europe. Hong Kong is, however, steadily upgrading its product quality. Last year, for example, US imports of all finished goods from Hong Kong increased by only about 3% in volume while the value went up by more than double that rate.

12. The only other important textile product exported to the United States is cotton fabric. Exports of cotton fabric amounted to about \$31 million last year, or about 10% of the colony's textile exports to the United States. The colony has about 18% of the US cotton fabric import market, ranking next to Japan in importance. Sales of cotton fabrics to the United States are controlled by the Long-Term Cotton Textile Agreement, which generally limits the volume growth in such exports to 5% annually. During most of the 1960s, however, Hong Kong was able to increase shipments by substantially more than this, partly because some items were uncontrolled or allowed to increase faster than 5%. Consequently, between 1964 and 1968 the volume of cotton textile sales actually grew by about 11% a year. Since 1968, however, Hong Kong, like Japan, has been unable to meet its full quota as it shifted operations more and more to synthetics. In 1969, shipments of cotton textiles rose by less than 3% and in 1970 declined by almost 9%. Because higher-quality items are being shipped, however, their value declined only 3% last year.

13. The United Kingdom and West Germany are also important markets for Hong Kong. Last year the United Kingdom took about \$150 million in textiles – about half the US level – while sales to West Germany amounted to about \$105 million. The UK share has fallen sharply, however, as sales to that market since 1965 have grown at only half the rate for overall textile exports. Last year, exports to the United Kingdom actually declined. Sales to West Germany, on the other hand, jumped 20% in 1970 and now account for about 11% of the total. Exports to other European Community countries are very small – about \$20 million annually – because of their restrictions on textile imports, which are much stiffer than West Germany's. Sales to other European countries have increased but constitute less than 5% of the total.

14. Pacific Basin countries other than the United States take a small but growing share of Hong Kong's textile exports. Sales to Australia and

CONFIDENTIAL

CONFIDENTIAL

Canada are running about \$30 million annually and are increasing by 15% to 20% annually. Exports to Japan increased by more than 100% last year. Even so, the Japanese market still takes less than \$20 million a year in textiles from Hong Kong, or about 2% of Hong Kong's total textile exports.

15. While Japan imports only small amounts of textiles from Hong Kong, it supplies one-half of Hong Kong's imports of manufactured textile products, valued at \$490 million. About one-third of Hong Kong's \$30 million worth of textile machinery imports also come from Japan. Total exports for the textile industry from Japan have grown by about 150% since 1965, and most of the increase has consisted of purchases of synthetic fibers, yarns, and fabrics. The natural fiber industry also depends on imports. Purchases of raw cotton and wool last year amounted to some \$100 million, about 10% of which came from the United States.

Problems

16. Despite the rapid progress over the past decade, Hong Kong's textile industry faces numerous problems. The principal long-term problems are rising wage rates and increasing competition for foreign markets from newcomers such as South Korea and Taiwan. Wage rates in Hong Kong's textile industry have increased sharply in recent years, largely because of the growing labor shortage brought on by the rapid expansion of the economy. In the past, labor was plentiful because of the inflow of refugees from Communist China, but this inflow has essentially stopped, and the growth rate of the industrial labor force has declined in recent years from 14% in 1968 to 5% in 1970. With the growing demands on the labor force, textile wage rates since 1965 have risen by about 10% annually, and in 1970 a hike of nearly 20% was registered. Pay scales in Taiwan and South Korea are more than 50% lower than those in Hong Kong, giving them a substantial advantage over the colony in the labor-intensive textile industry.

17. Hong Kong's response to this competition has been to press its modernization efforts and to shift into new and higher-quality product lines. So far this approach has kept exports growing rapidly even though Hong Kong has been edged out of some markets that formerly bought its low-quality, low-value items. Like the Japanese, who face a similar problem, some Hong Kong textile manufacturers are beginning to set up operations elsewhere in Southeast Asia where wage rates remain very low. Two textile mills are planned in Indonesia, for example, and plans are under way for a joint venture in Malaysia.

18. Restrictions on access to the US market are the most immediate problem facing the industry. Hong Kong has long had restrictions on its

CONFIDENTIAL

CONFIDENTIAL

cotton textile exports to all major markets as well as controls on all textile exports to non-US markets, including Japan and the EC countries. Because of these restrictions, and because the US market has accounted for nearly 40% of the increase in Hong Kong's textile exports since 1965, the colony consistently refused to reach agreement with the United States on the question of limiting woolen and manmade fiber textile exports to the US market. In September 1971, however, Hong Kong adjusted its position and announced plans to implement its own unilateral restraint program.

19. Under the new restraint program, effective 1 September 1971, the volume of textile shipments to the US market will be limited to a growth rate of about 6% annually, at least during the first year of the program. In effect, the program is an extension of the Long-Term Cotton Textile Agreement and, thus will cover all textile fiber products, including cottons, woolens, and manmade fibers. The program, however, calls for practically full shifting between textile categories, a loophole which greatly waters down its effect. Shipments of cottons and woolens have already begun to stagnate, and last year actually declined by 9% and 18%, respectively. This decline about offset the 30% increase in shipments of manmade fiber products, and overall textile shipments remained virtually unchanged from the 1969 level.

20. Unilateral export restraints, therefore, are not likely to have a significantly adverse effect on Hong Kong's textile industry. So long as shifting is allowed, exports of manmade fiber products can continue to increase substantially. Should US import demand for cottons and woolens continue to stagnate or decline, as seems likely, exports of manmade fiber products can increase at near recent rates. Moreover, Hong Kong will be able to increase the value of its textile exports to the US market by upgrading its product lines, a trend that has been taking place in recent years. Since 1965, the value of Hong Kong's exports has increased an average of almost 50% faster than the volume, and during the first five months of 1971 the value of US imports from Hong Kong rose by about 22% in contrast to the less than 9% increase in volume. If these trends continue, Hong Kong's textile exports to the US market could easily reach on the order of \$500 million by 1975, and, if exports to other foreign markets grow at the same rate as in the past five years, overall textile sales would amount to about \$1,600 million by the mid-1970s. This would represent a roughly 12% annual growth rate, compared with the 15% achieved between 1965 and 1970.

21. The overall economy probably would not be affected materially by such a slackening in the growth rate for textile exports. Non-textile exports have been growing by more than 20% annually in recent years and are expected to reach nearly \$3 billion in 1975. With the anticipated increase

CONFIDENTIAL

CONFIDENTIAL

in textile sales, total exports can be expected to amount to over \$4.5 billion by 1975, or more than double last year's level. The expansion of the economy required to achieve this level of exports would be only marginally less than the growth rate achieved during 1966-70. Slower growth in textile sales to the United States, therefore, does not appear to be a serious threat to Hong Kong's prosperity.

CONFIDENTIAL

CONFIDENTIAL

APPENDIX B

Taiwan's Textile Industry

Size and Scope

1. In the 1960s, Taiwan developed into the second largest textile exporter among less developed countries, ranking behind only Hong Kong. Textile exports rose from only \$21 million in 1960 to \$422 million in 1970, when Taiwan accounted for close to one-fifth of total textile exports by the less developed countries. The dynamism of Taiwan's textile industry is reflected in the rapid movement into synthetic fiber production. Except for South Korea, Taiwan is moving faster than any other less developed country in this direction and is the largest exporter of synthetic fiber products among these countries.

2. Taiwan's textile boom is based largely on its ample supply of exceptionally cheap labor. Wages in the textile industry are among the lowest in East Asia, enabling Taiwan to undersell its main competitors, Japan and Hong Kong, in many items. A second factor in the industry's rapid growth is the substantial foreign involvement. Both US and Japanese firms have provided technical assistance, and Japanese firms have invested directly in more than two dozen firms. Overseas Chinese are also major investors, but the extent of their participation is not precisely known. In addition, the Japanese have facilitated the industry's growth by means of production contracts and special marketing arrangements which utilize their established commercial channels. In fact, the Japanese probably have a larger stake in Taiwan's textile industry than in Hong Kong's or South Korea's.

3. Rapid growth in the 1960s made textiles the single most important manufacturing industry. Textiles account for about one-fifth of the value of manufacturing output and employ nearly 200,000 persons, representing about one-fourth of the manufacturing labor force. Some 2,100 registered factories are engaged in textile production, and the number of unregistered firms may well match this figure. The industry's spinning and weaving branches are dominated by a few large, modern mills, although many small firms are also involved. The apparel industry, however, still consists basically of small, family-type operations.

4. Although textiles is Taiwan's leading industry, its importance as a growth stimulus is gradually diminishing. Taiwan is developing manufacturing activities in an effort to maintain the impressive 10% real growth rate of the 1960s. In recent years, several new industries, especially

CONFIDENTIAL

electronics, electrical equipment, telecommunications equipment, and shipbuilding, have emerged. Output of electrical machinery, for example, has been growing by more than 50% annually since 1968, while output of electrical equipment and telecommunications equipment has increased by roughly 30% annually. These rates exceed the still very rapid growth rate of 25% registered by textiles. In exports, textiles are continuing to increase their share of the total, accounting for about 30% in 1970, but new products such as electronic articles are fast emerging as major export items.

5. The textile industry is rapidly expanding plant capacity and modernizing equipment. Between 1968 and 1970 the number of spindles and looms in operation each increased by 50% to 1.5 million and 36,000, respectively. Taipei estimates that between 1969 and 1972 more than \$230 million will be invested in new machinery and equipment. Much of the investment is geared to increasing output of synthetic fiber textiles, including clothing. Meanwhile, the government is promoting development of Taiwan's petrochemical industry to provide more raw materials and intermediate inputs for synthetic fiber production. The goal is to achieve virtual self-sufficiency in synthetics, from raw materials and fibers to finished products, as soon as possible.

Production Trends

6. Expansion of Taiwan's textile industry has accelerated since 1965, with average annual output gains of more than 26% as against 9% in previous years. The boost in output reflected the industry's growing emphasis on production for export. Since 1965, exports have accounted for over 85% of the increase in production, and by 1970 more than 60% of textile output was exported, compared with only 15% in 1960.

7. Synthetics and blends are becoming increasingly important in textile production (see Table B-1). Output of pure synthetic yarns and fabrics has jumped to a level of about six times that of 1965. Manmade materials - rayon, synthetics, and blends - now make up about one-fourth of fabric production and an even higher share of yarn production. Their share of total textile production has more than doubled since 1965, and a further rise is expected because of Taiwan's expanding production capacity. Output of synthetic fibers - mainly polyester and nylon - grew from virtually nothing in 1965 to over 57,000 tons in 1970, and plant capacity is continuing to expand rapidly. Moreover, the number of spindles devoted to manmade fibers has more than doubled since 1968 to almost one-third of the total, and about 10% of all looms are used for manmade and mixed-fiber fabrics.

CONFIDENTIAL

8. In contrast to other East Asian textile producers, Taiwan is increasing its output of natural fiber products as well as synthetics. Pure cotton fabric production, which makes up about three-fourths of total output, rose by about 85% between 1965 and 1970, including a 20% increase last year. This advance reflects increased domestic demand and Taiwan's ability to sell in markets once dominated by Japan. About one-half of Taiwan's cotton fabric production is now exported. Wool fabric output has also increased sharply but accounts for only a very small share of total fabric production.

9. Like the rest of the industry, Taiwan's garment business is undergoing rapid changes in its product lines. In the knitting sector, the mainstay of the garment industry, shirts, sweaters, and trousers are among the major items produced, and the trend is toward using fiber blends in these products. Indeed, output of knitted cotton shirts and trousers has declined since 1968, while those of woolen and manmade fibers continued their rapid growth. Production of woolen shirts rose from about 2 million pieces in 1965 to 18 million in 1970, and manmade fiber knitwear also recorded spectacular production gains. In woven apparel, the major items also include shirts, trousers, and ladies' dresses. The garment sector still deals in generally low-quality items, but product lines are gradually being upgraded with the help of foreign assistance. The Japanese already have several large apparel plants operating in Taiwan.

Trade Trends

10. Clothing is now Taiwan's major textile export in contrast to the mid-1960s when yarns and fabrics predominated (see Table B-2). Clothing sales have been booming; since 1965 their value has increased from \$18 million to about \$225 million. The largest jump occurred last year when a gain of nearly \$100 million was registered. Moreover, an increase of at least that much is likely in 1971, as half-year apparel exports stood at 80% of the 1970 level. Exports of fabrics, mostly cotton, are also increasing rapidly, reaching \$98 million last year compared with \$22 million in 1965. Synthetic fabrics are becoming more important, constituting about one-sixth of total fabric exports. Sales of synthetic yarn, valued at about \$38 million last year, make up almost half of yarn exports. Altogether, synthetics and other manmade fiber products account for at least half of total textile exports.

11. The United States takes the largest share of Taiwan's textile exports - about \$160 million worth in 1970, or 38% of the total. Between 1965 and 1970, sales to the US market increased by about 55% annually, accounting for about 40% of the growth in textile exports during that period. Last year alone, exports to the US market jumped about 60%.

CONFIDENTIAL

CONFIDENTIAL

Taiwan's share of US imports of manufactured textile products is now 7%, having risen from 2% in only five years. This is the largest share increase of any major textile exporting country selling in the United States.

12. Nearly all of Taiwan's textile exports to the US market -- about \$150 million worth in 1970 -- are clothing items (see Table B-3). Taiwan now ranks behind only Japan and Hong Kong as a source of US clothing imports; in 1970 its share was about 12%. Taiwan dominates the US import market for some items -- for example, knit trousers (51% of the total), knit shirts (41%), woven suits (43%), and pajamas (60%). The single most important items sold to the United States are sweaters, which constitute about one-fourth of total sales and, together with knit trousers, account for well over half of the increase in clothing sales to the United States since 1968.

13. Among Taiwan's other major textile markets, Hong Kong takes 13% of total textile exports, about the same as in 1965, although the value of exports to the colony increased from \$8 million to nearly \$60 million. These exports consist mostly of synthetic fibers, yarns, and fabrics for use in the colony's garment industry. Sales to Japan increased from about \$500,000 in 1965 to nearly \$40 million last year, when they made up 9% of the total. Almost half of these exports are clothing, and the balance consists mainly of cotton fabrics. Exports to EC countries are growing but still account for only about 6% of the total. Taiwan's other textile markets include Singapore, Indonesia, Australia, and Canada.

14. Taiwan gets 90% of its manufactured textile products imports from Japan, which supplied textile goods valued at about \$90 million in 1970. Most purchases from Japan consist of synthetic fibers, yarns, and fabrics. In addition, Japan accounts for most of Taiwan's textile machinery imports -- \$27 million last year. In 1970, textile imports from the United States, mostly cotton raw materials, amounted to about \$23 million.

Problems

15. The major problem now facing Taiwan's textile industry is the prospect of new limits on access to the US market. Exports of cotton textiles are already controlled under the Long-Term Agreement, and negotiations with the United States have been under way to limit the growth in manmade and woolen textile sales. Taipei has been somewhat more forthcoming in negotiations with the United States than other East Asian producers and in late May 1971 agreed in principle to restrict exports. At that time the understanding apparently called for an 11% growth rate in the volume of shipments during the first year of restrictions, with growth rates for the next two years of 10% and 9%, respectively. Several factors,

CONFIDENTIAL

CONFIDENTIAL

however, have slowed progress toward a final agreement, including the US failure to persuade South Korea and Hong Kong to limit their exports. Questions such as the base year to be used in any restraint program and the issue of shifting quotas between textile product categories are apparently still at issue.

16. A slower growth in sales volume to the United States to around 10% annually would not seriously hurt Taiwan's textile industry. This judgment is reflected in the fact that Taipei has already indicated its willingness to limit itself to around a 10% growth rate if other East Asian countries do the same. Given its strong competitive position, Taiwan should be able to sell increasing quantities of textiles in other overseas markets, although the very rapid 40% annual increase in exports to non-US markets can be expected to slow, especially if countries such as Japan clamp down on imports. But even if this growth rate drops to only 15% a year, sales outside the US market would still reach \$500 million by 1975. Meanwhile, the US market would continue to grow, although more slowly, reaching at least \$250 million by 1975 if 1970 were the base year for export controls. This figure would be substantially higher -- at least \$375 million -- if the base period were 1971, because Taiwan projects a whopping \$100 million increase in sales to the US market this year. Thus, even with added trade restrictions, the industry will still have plenty of opportunity to expand in the coming years.

17. Taiwan's overall economy is expected to do well even if textile sales slow considerably.⁽¹⁾ The government continues to place increased emphasis on developing basic industries and technology-intensive manufacturing activities, and substantial progress in this direction is already being made. For example, Taipei's projections indicate that electronics products will become the principal export item within a few years. The country's economic well-being basically depends on its ability to attract large amounts of foreign capital and technological know-how for use in developing new sophisticated export-oriented industries. So far it has been able to do this without much trouble. In the late 1960s, foreign capital inflows were running at about \$120 million annually, compared with only about \$35 million a year in the mid-1960s. As long as these inflows continue, the economy will do well.

1. even if textile exports to the US market were limited to only a 5% annual increase, the country's overall trade picture would not change appreciably. Total exports during 1972 and 1973 would grow by as much as 22% annually and Taiwan would maintain its favorable balance-of-payments position.

25X1

CONFIDENTIAL

Table B-1
Taiwan: Textile Production

	<u>1961</u>	<u>1965</u>	<u>1968</u>	<u>1969</u>	<u>1970</u>
	<u>Metric Tons</u>				
Yarns and fibers					
Cotton and blended cotton yarn	48,910	56,614	82,370	96,291	103,804
Woolen and blended woolen yarn	606	1,674	4,832	4,921	8,505
Synthetic fibers and filament	0	1,345	20,789	33,938	57,346
Rayon fibers and filament	4,087	5,131	20,461	21,839	24,888
Synthetic yarn	0	525	1,558	1,976	3,597
Rayon yarn	5,627	12,321	19,997	22,913	27,904
<i>Total</i>	<i>59,230</i>	<i>77,610</i>	<i>150,007</i>	<i>181,878</i>	<i>226,044</i>
	<u>Thousand Square Meters</u>				
Fabrics					
Cotton (pure)	200,105	268,018	371,405	415,841	495,966
Cotton blends	216	1,875	13,111	26,655	49,381
Woolen	1,084	2,802	4,233	4,139	5,151
Synthetic <u>a/</u>	0	7,312	40,424	43,396	52,239
Rayon <u>a/</u>	14,171	31,811	54,384	63,165	64,894
<i>Total</i>	<i>215,576</i>	<i>311,818</i>	<i>483,557</i>	<i>553,196</i>	<i>668,131</i>
<i>a. Including blends.</i>					

a. Including blends.

CONFIDENTIAL

Table B-2
Taiwan: Textile Exports

	Million US \$						
	1960	1965	1966	1967	1968	1969	1970
<i>Total</i>	21.1	64.1	86.1	130.8	133.7	257.5	421.7
Of which:							
Yarns	2.3	20.4	26.1	30.6	29.3	50.8	78.5
Fabrics	11.6	21.5	27.8	41.6	53.4	69.4	97.8
Non-clothing products	2.6	3.5	5.8	11.4	13.0	14.8	17.8
Clothing	2.4	18.3	24.9	46.7	96.7	127.6	224.3
Fibers	N.A.	0.4	1.5	0.5	1.3	4.9	3.3

Table B-3
Taiwan: Textile Exports to the United States

	Million US \$						
	1960	1965	1966	1967	1968	1969	1970
<i>Total</i>	3.0 <u>a/</u>	18.3 <u>a/</u>	20.2 <u>a/</u>	35.6	66.9	102.0	161.0
Yarns, fabrics, and non-clothing products	N.A.	6.0 <u>a/</u>	6.0 <u>a/</u>	7.7	8.1	10.7	11.0 <u>a/</u>
Clothing	N.A.	12.3	14.2	27.9	58.8	91.3	150.0 <u>a/</u>

a. Estimated.

CONFIDENTIAL

- 27 -

CONFIDENTIAL

CONFIDENTIAL

APPENDIX C

South Korea's Textile Industry

Size and Scope

1. South Korea's development as a major textile exporter has been exceptionally rapid. Foreign sales climbed from only \$3 million in 1960 to \$324 million in 1970, and South Korea now ranks third -- behind Hong Kong and Taiwan -- among the less developed countries as an exporter. These achievements have been largely due to a massive inflow of foreign capital and know-how. Since 1960, more than \$200 million in foreign capital, mostly private loans, has gone into the textile industry. The Japanese have been the chief source of foreign capital, and through contract arrangement they have provided much of the crucial marketing skills needed by the industry as a newcomer to the export business.

2. The textile industry is easily the most important in South Korea, accounting for about 25% of total manufacturing output and about 40% of export earnings. With some 240,000 workers -- roughly three-fourths of them women -- textile production accounted for about 30% of the manufacturing labor force in the late 1960s. The country's 950,000 spindles are operated by about 220 mills, but a few firms account for a large share of total spindlage. Some 1,300 firms in the weaving sector operate 32,000 looms. Garment making involves some 4,000 firms employing a total of about 75,000 persons, or one-third of the textile labor force.

3. Textiles were a major factor in stimulating South Korea's economic expansion during the latter 1960s, when real gross national product (GNP) grew at an extraordinary average rate of 9.5% annually. The country, however, is now developing new industries to help sustain its economic growth. Since 1967, for example, exports of chemicals and machinery have increased by 380% and 330%, respectively, and similar growth was registered by a wide range of other manufactured products. Textile exports, on the other hand, have grown by about 160%, and their share of total foreign sales consequently has begun to decline slightly. Textiles are still an important growth industry, however, and accounted for more than one-third of the increase in manufacturing output last year.

Production Trends

4. Most of the growth in textile production occurred during 1966-70, when the industry's output increased by 32% annually. This is in marked

CONFIDENTIAL

contrast to the 8% annual growth rate recorded between 1960 and 1965. At that time the industry was engaged mainly in producing cotton and woolen textiles, but since then there has been a dramatic shift to synthetics and synthetic blends (see Table C-1). Indeed, synthetics accounted for virtually all the growth in yarn and fabric production between 1965 and 1970. Their share of both yarn and fabric output during that period jumped from only about 5% to roughly one-third last year. Synthetic fabric production alone has averaged a whopping 45% annual increase since 1965.

5. The industry is pushing fast to accelerate the trend toward synthetics. Plant capacity for synthetic fibers is expanding rapidly and by the end of 1971 is expected to reach at least 90,000 tons annually, compared with only about 15,000 tons in 1968. Plants producing synthetic fibers will number about 15, compared with only 6 in 1968. Supporting this tremendous expansion is the country's rapidly growing petrochemical industry which is providing needed intermediate products. The industry nevertheless still has to import large quantities of synthetic fibers and fabrics to meet its needs. Last year, for example, net imports of synthetic fabrics were equal to about 70% of domestic production. A large share of synthetic fiber supplies also came from overseas.

6. While synthetics are booming, output of almost all natural fiber textiles is declining. Cotton fabric production -- once the industry's mainstay -- has fallen by 16% since 1965 and now accounts for about one-half of total fabric output, compared with 74% in 1965. The major problem is that domestic demand has been dropping off because of a shift to synthetics. South Korea has been able to take up part of the slack by increasing overseas sales, and now about three-fourths of cotton fabric output is exported. Production of pure woolen textiles has also declined sharply -- by about 42% since 1965 -- although increased production of wool and synthetic blends has more than made up the loss. This change reflects primarily increased domestic demand; exports take roughly 20% of total woolen fabric production, or about the same share as in 1965. In contrast to the other natural fibers, raw silk production has boomed since 1965, with increases of about 22% annually. South Korea is now the world's largest raw silk exporter.

7. South Korea's garment industry has expanded very rapidly with the shift to synthetics. Most of the output is for overseas markets, and exports of clothing and accessories have been growing by more than 55% annually since 1965. The industry produces mainly knitwear, concentrating on such items as sweaters, gloves, hosiery, and underwear. Production of sweaters -- almost all made of synthetic yarns -- rose from 6 million pieces in 1965 to about 90 million pieces last year. By and large, these knitwear articles are low-value items that the industry has had no trouble selling.

CONFIDENTIAL

CONFIDENTIAL

The same holds true for woven apparel products, which consist mainly of men's and boys' garments – especially low-quality shirts. In addition to these finished products, the industry produces large amounts of clothing accessories such as dress shields, shoulder pads, and pockets.

Trade Trends

8. Textile exports have increased by a spectacular 500% over the past five years and amounted to about \$324 million (see Table C-2). Most of the increase since 1965 has been in clothing and accessories, which now make up about two-thirds of total textile exports. Exports of these items have jumped about ninefold since 1965 and were valued at more than \$200 million in 1970. Most of the finished goods consist of manmade fibers or synthetic blends. Fabric exports amounted to about \$54 million last year – about 17% of total textile exports. Sales of cotton fabrics, which have more than doubled since 1965, make up about half of total fabric exports. In addition, South Korea has developed substantial exports of raw silk. Last year such sales amounted to \$39 million, compared with only \$1 million in 1965.

9. Almost one-half of South Korea's textile exports – or \$149 million worth in 1970 – go to the US market. Sales to the United States grew nearly fivefold between 1965 and 1970, an increase exceeded only by Taiwan among major textile exporting countries. Last year, exports to the United States jumped by 30%, and over the past five years, South Korea has increased its share of the US import market from 2% to 6%. Despite the phenomenal growth in sales to the United States, textiles are of declining importance in South Korean - US trade because exports to the United States of other items such as electronic products are increasing even faster. In 1965, textiles constituted about 41% of total South Korean exports to the United States, but by 1970 the share had dropped to 38%.

10. Nearly 90% of South Korea's textile exports to the US market consist of clothing and accessories (see Table C-3). In the process of boosting its exports, South Korea has captured about 9% of the US import market for finished goods. This was basically accomplished by concentrating on inexpensive products in which South Korea could considerably undersell its major competitors – Japan and Hong Kong. South Korea, for example, is now the leading supplier of manmade fiber knit underwear (50% of US imports), hosiery (28%), and T-shirts (68%) -- all relatively low-priced items. South Korea also accounts for a large share – about 30% -- of US imports of sweaters made of manmade fibers. These are usually inexpensive ones – the average US import price for South Korean sweaters in 1970 was about \$14 per dozen or more than 10% below the average for manmade sweaters imported from other countries. In addition to clothing, South Korea sells

CONFIDENTIAL

CONFIDENTIAL

small amounts of fabrics in the US market, which make up only 9% of total textile exports to the United States.

11. While the US share of South Korea's textile exports has been stagnating, that of Japan has been increasing rapidly. In 1965, Japan took less than \$3 million worth of textiles -- about 5% of total South Korean textile exports -- but by 1970 the value had risen to \$96 million -- or 30% of South Korean textile exports. In contrast to the United States, however, Japan purchases mainly raw silk and clothing accessories. Because of Tokyo's desire to protect its own clothing industry, the Japanese import relatively little ready-to-wear clothing.

12. Exports to other foreign markets have also increased appreciably, but their share of total textile sales nonetheless has declined sharply since 1965 because of booming sales to the United States and, especially, Japan. Exports to these other countries amounted to about \$80 million last year, compared with less than \$25 million in 1965. Hong Kong is one of the more important customers, taking a substantial share of synthetic fabric shipments -- 50% in 1969. Exports to European Community countries rose considerably during the late 1960s, but by 1969 they still took only about 6% of total textile sales. The problem is that South Korea, as a relatively new textile exporter, has been unable to capture much of the EC's highly restricted import market. Even in the case of countries such as Canada, Korea has had to bargain hard just to get a foothold in the market.

13. Japan now accounts for more than 90% of Korean imports of manufactured textile products. About 80% of these purchases consist of synthetic fibers and fabrics, imports of which come largely from Japan. Japan is also the major supplier of textile machines, selling about \$35 million worth in 1970. Imports of textile products from Japan increased from \$39 million in 1965 to \$150 million last year, a 31% annual increase. Imports for the natural fiber industry, on the other hand, come largely from the United States. Textile imports from the United States have increased about 10% annually since 1965, reaching \$68 million in 1970. About 90% of this trade consists of raw cotton.

Problems and Prospects

14. The darkest cloud on the textile industry's horizon is the prospect of restraints on sales to the United States. Such controls would hurt South Korea more than any other East Asian producer. Although developing rapidly, the South Korean industry is still in its infancy and any sharp slowdown in sales growth would undoubtedly upset development plans and hold the industry below its potential. Moreover, the heavy reliance on borrowed capital requires maintenance of high sales growth rates to meet

CONFIDENTIAL

CONFIDENTIAL

debt obligations. An unplanned slowdown without considerable debt relief would lead to numerous bankruptcies.

15. Although export controls on sales to the US market clearly would hit the textile industry hard, they would not necessarily cripple it. Restrictions are usually based on the volume of shipments, and if these were allowed to grow by only 10% annually -- a figure used in US negotiations with Taiwan -- it would represent a substantial decline from the roughly 20% growth rate achieved in 1970. The value of exports, however, would presumably increase much faster because of the possibility of shifting to higher-value export items. South Korea, as well as Taiwan, is in an especially good position to make such shifts because it now concentrates primarily on low-value items. Moreover, the longer it takes to reach a final agreement, the better the textile industry will fare under export controls. Exports to the US market are still booming -- growing by roughly 80% in the first half of 1971 -- and, consequently, if 1971 serves as the base period, future exports would be substantially higher than if 1970 were the base period.

16. How deeply the South Korean textile industry will be hurt by export controls will also depend on what happens in its other major markets, especially Japan. Japan has accounted for more than one-third of the increase in textile exports since 1965. If sales to Japan continue to grow at near the pace of recent years, the South Korean industry probably would be able to overcome the adverse effect on limits in the US market without too much trouble. However, Tokyo is under pressure from its producers for protection from foreign competition. If sales to Japan grow at only half the rate of recent years and exports to the US market increase by only 10% a year in value, overall textile exports to the world would still manage to more than double over the next five years. Textile export growth would be substantial, averaging between 15% and 20% annually.

17. In general, South Korea faces the problem of obtaining sufficient foreign exchange to continue its rapid economic growth and repay its increasing foreign debt obligations. Even a small slowdown in export growth during the next few years thus could result in a major balance-of-payments problem. To avoid import restrictions and a resulting slackening of economic growth, Korea would have to obtain debt relief or additional foreign aid. This will largely depend on Seoul's ability to negotiate a rescheduling of its outstanding foreign debt and the ability of the local private firms to roll-over their loans with US and other foreign banks. Given the dynamism of the current economy, such private debt forbearance would be obtained with relatively little trouble. Financial assistance -- both official and private -- would be available especially from Japan which has a large economic stake in South Korea.

CONFIDENTIAL

Table C-1

South Korea: Textile Production

	<u>1960</u>	<u>1965</u>	<u>1968</u>	<u>1969</u>	<u>1970</u>
	<u>Million Metric Tons</u>				
Yarns					
Cotton	49,142	65,027	51,919	64,712	71,937
Woolen and worsted	2,135	4,655	5,812	5,043	3,696
Raw silk	297	754	1,545	2,075	2,027
Synthetic fiber	0	1,915	7,377	19,754	34,875
Rayon	0	0	4,241	4,637	5,318
<i>Total</i>	<i>51,574</i>	<i>72,351</i>	<i>70,894</i>	<i>96,221</i>	<i>117,853</i>
	<u>Thousand Square Meters</u>				
Fabrics					
Cotton	126,121	222,879	113,746	191,720	186,360
Woolen	3,642	4,590	2,504	2,731	2,682
Silk	3,060	3,993	3,183	4,703	6,921
Synthetic	3,922	18,301	71,001	96,480	117,852
Rayon	52,232	51,860	35,251	41,724	47,938
<i>Total</i>	<i>188,977</i>	<i>301,623</i>	<i>225,685</i>	<i>337,358</i>	<i>361,753</i>

CONFIDENTIAL

- 34 -

CONFIDENTIAL

Table C-2
South Korea: Textile Exports

	Million US \$					
	<u>1960</u> ^{a/}	<u>1965</u>	<u>1967</u>	<u>1968</u>	<u>1969</u>	<u>1970</u>
<i>Total</i>	3.4	52.5	123.9	190.1	249.5	323.9
Of which:						
Yarns	0	2.3	3.1	3.9	5.6	13.2
Fabrics	2.4	17.8	30.8	40.2	44.0	53.5
Non-clothing products	0	4.0	13.7	13.9	12.4	12.6
Clothing products	0	20.7	59.2	112.2	160.6	202.2

a. *Estimated.*

CONFIDENTIAL

- 35 -

CONFIDENTIAL

Table C-3

South Korea: Textile Exports to the United States

	Million US \$					
	<u>1960</u> ^{a/}	<u>1965</u>	<u>1967</u>	<u>1968</u>	<u>1969</u>	<u>1970</u>
<i>Total</i>	<i>N.A.</i>	<i>25.3</i>	<i>46.6</i>	<i>89.2</i>	<i>114.2</i>	<i>148.8</i>
Of which:						
Yarns	0	Negl.	0.2	0.1	0.1	0.3
Fabrics	N.A.	5.8	7.8	9.8	10.0	13.4
Non-clothing product	0	0.6	1.4	1.0	1.2	1.8
Clothing products	0	12.2	30.7	70.8	98.1	131.1

a. Estimated.

CONFIDENTIAL

CONFIDENTIAL